



ARIZONA STATE RETIREMENT SYSTEM

3300 NORTH CENTRAL AVENUE • PO BOX 33910 • PHOENIX, AZ 85067-3910 • PHONE (602) 240-2000

7660 EAST BROADWAY BOULEVARD • SUITE 108 • TUCSON, AZ 85710-3776 • PHONE (520) 239-3100

TOLL FREE OUTSIDE METRO PHOENIX AND TUCSON 1 (800) 621-3778

EMAIL ADDRESS: ASKMAC@AZASRS.GOV • WEB ADDRESS: WWW.AZASRS.GOV

Paul Matson
Director

MINUTES REGULAR MEETING ARIZONA STATE RETIREMENT SYSTEM BOARD

Friday, October 16, 2009
8:30 A.M., MST

The Arizona State Retirement System (ASRS) Board met in the 10th Floor Board Room, 3300 N. Central Avenue, Phoenix, Arizona. Mr. David Byers, Chair of the ASRS Board, called the meeting to order at 8:36 AM, MST.

The meeting was teleconferenced to the ASRS office at 7660 E. Broadway, Tucson, Arizona 85710.

1. Call to Order; Roll Call; Opening Remarks

Present: Mr. David Byers, Chair
Mr. Tom Connelly, Vice-chair
Mr. Jaime Gutierrez
Mr. Chris Harris
Dr. Keith Meredith
Mr. Michael Townsend
Mr. Larry Trachtenberg (arrived at 8:37 A.M.)
Mr. Steve Zeman

Absent: Mr. Jim McLaughlin

A quorum was present for the purpose of conducting business.

Mr. Larry Trachtenberg arrived at 8:37 A.M.

2. Presentation Regarding the PRIDE Award for Diversity

Mr. Paul Matson, Director, and Mr. Anthony Guarino, Deputy Director and Chief Operations Officer, presented the PRIDE Award for Diversity to the ASRS Records Management, Imaging and Mail Room Team. The Team was nominated by their peers as being committed to diversity. The team exemplifies the PRIDE qualities of diversity: *"I treat all people fairly and without judgment. I take the time to listen and to understand. I respect diversity knowing that our differences enrich us all. I build relationships and recognize the efforts of others."* The members of the Records Management, Imaging and Mail Room Team are: Joy Fuentes, Andrew Watkins, Kim Harding, Karen Moore, Grace Olmos, Nancy Fuller, John Mathine, Allison Moore, Tammy Wilson, and Kristi Zeller.

3. Approval of the Minutes of the September 18, 2009 Regular Session of the ASRS Board

Motion: Mr. Steve Zeman moved to approve the minutes of the September 18, 2009, Regular Session of the ASRS Board.

Mr. Michael Townsend seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

4. Presentation, Discussion and Appropriate Action Regarding the 2010 Legislative Session

Mr. Pat Klein, Assistant Director, External Affairs, and Ms. Lesli Sorensen, Government Relations Officer, addressed the Board regarding the 2010 Legislative Session. Mr. Jaime Gutierrez, Chair, External Affairs Committee (EAC), said it was being recommended that the legislative proposals be separated into two groups, one group to move forward immediately, the other group to conduct further research. Ms. Sorensen provided an overview of the 2010 legislative issues the EAC decided to move forward:

Long-Term Disability (LTD) Program: permit a person appealing an ASRS decision under the LTD Program to require that the ASRS Board hear the appeal in Executive Session.

Motion: Mr. Jaime Gutierrez moved to approve the Long-Term Disability (LTD) Program legislative initiative that allows a person appealing an ASRS decision under the LTD Program to allow that the ASRS Board hear the appeal in Executive Session.

Dr. Keith Meredith seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

Plan Design: modify Average Monthly Salary from 36 to 60 months (new hires only); modify Rule of 80 to Rule of 85 (new hires only); cap Employer Refunds at 25% (new hires only).

Ms. Sorensen noted the first two provisions of Plan Design legislation, 36 to 60 months and Rule of 80 to 85, cannot be supported by the Board, but to give information on the impact of the modifications to the Legislature.

Motion: Mr. Jaime Gutierrez moved to authorize the 2010 legislative initiative and the giving of information on the impact of the modifications dealing with Plan Design to modify Average Monthly Salary from 36 to 60 months (new hires only); modify Rule of 80 to Rule of 85 (new hires only); cap Employer Refunds at 25% (new hires only) effective July 1, 2011.

Dr. Keith Meredith seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

Return to Work (RTW) Option 1: Establish an Alternate Contribution Rate for Return to Work (RTW);

Motion: Mr. Jaime Gutierrez moved to approve the 2010 legislative initiative regarding Return to Work to establish an Alternate Contribution Rate.

Mr. Michael Townsend seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

Return to Work (RTW) Option 2: Repeal of Return to Work without Suspension of Benefits.

Motion: Mr. Jaime Gutierrez moved to approve the 2010 legislative initiative regarding the repeal of Return to Work without Suspension of Benefits.

Mr. Michael Townsend seconded the motion.

By a vote of 6 in favor, 2 opposed, 0 abstentions, and 1 excused, the motion was approved.

Technical and Federal Conforming Changes: incorporate Federal Conforming Changes.

Motion: Mr. Jaime Gutierrez moved to approve the 2010 legislative initiative regarding Technical and Federal Conforming Changes.

Mr. Tom Connelly seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

Ms. Sorensen provided an overview of the 2010 legislative issues that required additional research:

Administration: exempt the ASRS from AZNet, the Statewide telecommunications and network infrastructure program, subject to discussion with ADOA; permit the board to authorize appropriations to continue ASRS operations in the event the legislature fails to make an appropriation; permit the ASRS to charge interest, penalties and administrative charges for some functions, subject to discussion by the ASRS Board.

Benefits: raise the minimum benefit threshold for mandatory lump sum payouts.

Employer Administration: permit the ASRS to require an Employer to self-audit upon request.

Ms. Sorensen provided an overview of a 2010 legislative issue that another party has proposed, which could impact the ASRS.

Retiree Health Insurance: Prohibit public Employers from providing health insurance coverage to their retired employees, essentially requiring all public sector retirees to take only the ASRS Retiree Health Insurance Plan or private insurance.

Ms. Sorensen said the ASRS is neutral regarding this proposal. Health Insurance (HI) premiums would probably remain stable and there is likely little financial impact to the ASRS since additional enrollees would require the HI Vendor to provide the ASRS with additional staff.

Motion: Mr. Jaime Gutierrez moved to approve the ability of staff to negotiate the best legislative outcomes on the initiatives the Board already approved in previous motions.

Dr. Keith Meredith seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

Mr. Byers said he hoped staff was looking at some of the initiatives possibly being included in a special session; plan design and budget deficit being two examples.

Ms. Sorensen said the Legislature may go into a special session in late November.

5. Presentation, Discussion and Appropriate Action Regarding the ASRS Strategic Asset Allocation Study

Mr. Allan Martin, Managing Partner, New England Pension Consultants (NEPC) presented the ASRS Strategic Asset Allocation Study to the Board. Mr. Martin presented it to the Investment Committee (IC) on October 13, 2009. The IC recommended the Board approve the Asset Allocation Policy Schematic.

Recommended ASRS Asset Allocation Policy Schematic (Exhibit A)

Asset Class	Target	Range	Benchmark	Passive
PUBLIC EQUITY				
Large Cap	28%		S&P 500	75 +/- 20%
Mid Cap	6%		S&P 400	45 +/- 20%
Small Cap	6%		S&P 600	30 +/- 20%
US Equity	40%	(30 - 50%)		
Developed Large Cap	13%		MSCI EAFE	50 +/- 20%
Developed Small Cap	2%		MSCI EAFE Small Cap	20 +/- 20%
Emerging Markets	3%		MSCI Emg Mkts	20 +/- 20%
Non-US Equity	18%	(8 - 28%)		
FIXED INCOME				
Core	24%		Barclays Aggregate	55 +/- 20%
High Yield	2%		Barclays High Yield	20 +/- 20%
US Fixed Income	26%	(16 - 36%)		
PRIVATE EQUITY				
Private Equity	7%	(5 - 9%)	Russell 3000 + 3%	N/A
REAL ESTATE				
Real Estate	6%	(4 - 8%)	NCREIF + 1%	N/A
INFLATION LINKED ASSETS				
Commodities	3%	(0 - 5%)	TBD	N/A
TIPS	0%	(0 - 5%)	TBD	N/A
RISK PARITY				
Risk Parity	0%	(0-5%)	TBD	N/A
ABSOLUTE RETURN				
	0%	(0 - 5%)	TBD	N/A
OPPORTUNISTIC				
	0%	(0 - 10%)	TBD	N/A
TOTAL	100%			
GTAA	10%	(8-12%)	TF Benchmark	N/A
Expected Return	9.33%			
Standard Deviation	14.02%			
Sharpe Ratio	0.51			

*Risk Parity to be evaluated over the next 6 months

Total Fund Benchmark

28% S&P 500

6% S&P 400

6% S&P 600

13% MSCI EAFE

2% MSCI EAFE Small Cap

3% MSCI Emerging Markets

24% Barclays Capital Aggregate

2% Barclays Capital High Yield

7% Russell 3000 + 3%

6% NCREIF + 1%

3% TBD (Commodities)

Note: Indicators in bold are new to the Total Fund Benchmark

Motion: Mr. Tom Connelly moved to approve the recommendations of the ASRS Strategic Asset Allocation Study.

Mr. Chris Harris seconded the motion.

By a vote of 8 in favor, 0 opposed, 0 abstentions, and 1 excused, the motion was approved.

6. Presentation, Discussion and Appropriate Action Regarding the Implementation Plan for the Exemption of the ASRS from Arizona Department of Administration (ADOA) Personnel Management, Personnel Board Provisions, and the ADOA Classification and Compensation Statute

Mr. Paul Matson, Director, addressed the Board regarding the topic. He said the ASRS does not intend to rewrite all personnel rules simply as a result of the legislation that was recently passed which formally excluded the ASRS from the ADOA Personnel System. Rather, the ASRS management will utilize the ADOA and State personnel platform to the extent feasible if practical and effective for the ASRS. Exceptions will be made when prudent.

As a result of the exemptions, the ASRS is now considered a Non-System agency. State agencies are classified into System and Non-System groups. System agencies are required to adhere to State Personnel Management policies and procedures and they are required to adhere to the Personnel Board provisions for covered positions. Also, they must operate within the confines of the State's classification and compensation model for all positions whether covered or uncovered.

Non-System agencies are not required to operate under the State Personnel Management provisions; and due to the agency's positions established as uncovered, the agency is not required

to adhere to Personnel Board provisions nor must they operate within the State's classification and compensation model. However, an agency may choose to utilize any of these established practices and adopt them for their own either in part or in whole. This would include the utilization of current classifications and compensation ranges, personnel policies and procedures, and other practices should these meet the needs of the agency

Mr. Matson said possible changes in personnel management could, for example, allow the PRIDE committee and Human Resources to give PRIDE award recipients additional annual leave, if prudent. Additionally, for example, the ASRS would have authority to move a grade 21 employee to a grade 23, if their duties are consistent with that grade as determined ultimately by the ASRS management. The ASRS will still attempt to follow ADOA practices and consult with ADOA where practical, but is now able to make the final decision to reclassify that employee to grade 23 for example.

Mr. Gutierrez asked if a formally covered employee who might be facing disciplinary action or termination, had a grievance, where they would go, since they used to go to the Appeals Board. Mr. Matson noted the ratio of covered to uncovered employees at the ASRS is about 95 to 5, with only 5% of employees migrating from covered to uncovered status. Only 12 employees were affected, moving from covered to uncovered status. Out of those 12 employees, 11 people were awarded enhanced annual leave in the conversion, and the other employee's leave remained the same because they were already at the maximum amount. The amount of their annual leave had previously been based on seniority. Mr. Matson noted those 12 individuals did lose their right to appeal to the Appeals Board. However, the ASRS has a progressive four step discipline process that is generally utilized, including discussion, documentation, and written dissemination to the employee. In his history as Director, and his history at the ASRS, he said he was unaware of any appeal going to the Appeals Board from the ASRS. He said Human Resources was also unaware of such. Also, the perceived necessity to do an external appeal is often linked to political appointees. Some suggest that if the senior staff member was a political appointee at a state organization, he or she might possibly change or augment staff based on political position. However, the ASRS Director is appointed by an independent Board, and is not a political appointee.

7. Presentation, Discussion and Appropriate Action Regarding the FY 2009 ASRS Budget Reversions

Mr. Matson explained in keeping with the strategies the ASRS planned and implemented last year to reduce agency expenditures for FY 2009, significant reductions to the operating budget totaling \$1,585,700 (equivalent to 6.6% of the FY 2009 Appropriations) were realized in various categories of expenditure. In addition, \$446,000 (equivalent to 1.8% of the FY 2009 Appropriations) from funds appropriated in prior fiscal years was able to be returned to the ASRS Trust Fund. In total, \$2,031,700 (equivalent to 8.4% of the FY 2009 Appropriations), was able to be returned to the ASRS Trust Fund at the conclusion of FY 2009.

Mr. Matson said a major IT initiative spanning seven years had been implemented marginally under budget, also contributing to the savings being returned to the Trust Fund. He also said the ASRS would strive to continue potential savings in 2010, though they would likely be much more modest.

8. Director's Report

Mr. Matson presented the report to the Board. He said the ASRS planned a Continuity of Operations Plan (COOP) test, which was executed the previous day and involved approximately 23% of staff, to test the extent to which the ASRS workforce could telecommute. It is estimated that at least 40% of staff could telecommute with no significant negative effect on operations. Mr. Matson said 3% of staff has been on sick leave on average, and only 1/6th of those are estimated to have any type of flu.

Mr. Matson noted Luz Academy of Tucson was no longer delinquent.

Mr. Matson said, for decades, it was understood that System benefits have not been guaranteed. However, prior to making any reduction in benefits, the ASRS wanted a formal opinion from the Attorney General (AG). The ASRS has not yet received the opinion. Mr. Matson explained he planned to draft a letter to update all (approximately) 1,800 System members with respect to the status of system members accounts and benefits and outstanding legal opinion. He said if there were to be an AG decision, he wanted System members and the ASRS to have time to plan. Mr. Matson said he felt the earliest that any reduction in benefits could occur, if there were any reduction, would be in July 2010.

Mr. Matson reviewed the following topics on the draft agendas to be presented at the next two Board meetings: in November, Schedule B legislative analysis out of the External Affairs Committee; Plan, System, and LTD Valuations; Global Tactical Asset Allocation strategy presentation; governance and oversight regarding a new 403(b)/457 plan; in December, new 403(b)/457 plan vendor selection; Private Equity; Real Estate; Opportunistic; the Total Fund review; follow up regarding notification of newly found members.

Mr. Gutierrez asked about the forecast on the ASRS leases in Phoenix and Tucson. Mr. Matson said he would provide updated information via email to trustees.

9. Possible Presentation Regarding Board Committee Updates

Mr. Gutierrez, Chair, External Affairs Committee (EAC), said the next EAC meeting will take place November 6, 2009. The EAC will discuss the legislative items mentioned previously.

Mr. Tom Connelly, Chair, Investment Committee (IC), said the next IC meeting will take place November 16. The IC will look at the details of asset allocation.

Mr. Steve Zeman, Chair, Operations Committee (OC), said the next OC meeting will take place November 5, at which General Accounting, three-year strategic initiatives, and steering committee updates, would be discussed.

10. Board Requests for Agenda Items

There were no requests for agenda items.

11. Call to the Public

Mr. Uwe Fink addressed the Board regarding his views on health insurance legislation, the Arizona Science Foundation, and an article in the Wall Street Journal, regarding investments. Mr. Matson responded to the investments concern stating the general area of concern that has been referenced is not with direct marketing employees of a firm, but with third party marketers a firm may have hired. He said the ASRS has added disclosures to the due diligence process to determine if third party marketers are utilized. Mr. Harris noted the Investment Committee has discussed this topic over the past few months.

12. The next ASRS Regular Board meeting is scheduled for Friday, November 20, 2009, at 8:30 a.m., at 3300 N. Central Avenue, 10th Floor Board room, Phoenix, Arizona.

13. Adjournment of the ASRS Board

Mr. Byers adjourned the Board meeting at 10:38 AM.

ARIZONA STATE RETIREMENT SYSTEM

Lisa Hanneman
Board Secretary

Date

Paul Matson
Director

Date